SK M&E Bersekutu Sdn Bhd v Pembinaan Legenda Unggul Sdn Bhd (in creditors' voluntary liquidation) and another appeal

FEDERAL COURT (PUTRAJAYA) — CIVIL APPEAL NOS 02(f)-130–11 OF 2017(W) AND 02(f)-131–11 OF 2017(W)
RICHARD MALANJUM CHIEF JUSTICE, AHMAD MAAROP PCA, AZAHAR MOHAMED, ROHANA YUSUF AND ZAWAWI SALLEH FCJJ
12 MARCH 2019

Contract — Building contract — Retention sum held by employer — Whether pending its release, employer held retention sum on trust for contractor/subcontractor — Employer went into voluntary liquidation owing millions of ringgit in unpaid retention monies to numerous subcontractors — Whether subcontractors only had a claim in debt unless facts and circumstances strongly indicated that monies were held on trust for them by employer — Whether the law would not imply existence of a trust in absence of clear evidence to create a trust

The common respondent in the two appeals herein had separately engaged the two appellants to carry out subcontract work on two different building projects. The subcontracts between the parties allowed the respondent to deduct and hold 'retention monies' which were payable to the respective appellants in two tranches — the first, after issuance of a certificate of practical completion of the main contract; the second, after expiry of the defects liability period (or issuance of the certificate of making good defects). In both the appeals herein, the respondent failed to pay the retention monies it owed the appellants. At the time the respondent went under voluntary liquidation, it owed 128 of its subcontractors (including the appellants) unpaid retention monies amounting to RM8.2m. As the respondent had not opened any special bank account to hold the retention monies, the appellants applied to the High Court to order the respondent to deposit the retention sums it owed them into a separate account pending the final determination of arbitration and/or adjudication proceedings. The order was granted by the High Court on the ground the respondent held the retention sums on trust for the appellants although there was no express clause in the subcontracts for the creation of a trust. The Court of Appeal ('COA') set aside the order on appeal, ruling that no trust could be implied because, inter alia, the conduct of the parties did not show an intention to create a trust and the retention monies were also not specifically identifiable. The COA held that the respondent only had a contractual obligation to release the monies to the appellants when the conditions for their release had been satisfied. The Federal Court granted the

appellants leave to appeal against the COA's decision on the following questions of law: (a) whether until the conditions for the release of retention sums to a contractor under a building contract had been met, the law implied that the employer held the retention sums on trust for the contractor, and if the law did not so imply, then whether a trust existed or not depended on the construction of the contract; and (b) whether, in any event, a trust could exist if the employer had not set aside the retention monies in a separate fund. At the appeal hearings, the appellants argued that since the retention monies were only to be applied by the employer for the purpose of defect rectification and the balance was to be paid to them, they had a beneficial interest in the retention monies and it had to be implied that the employer held the monies on trust for them. The respondent, on the other hand, submitted that without express provisions for the creation of a trust, no trust could be implied. The respondent also pointed out that under insolvency law, all unsecured creditors were treated equally under the pari passu rule and it would breach that principle if the appellants' claims were given preference over those of the other creditors.

Held, unanimously dismissing the appeals and affirming the decision of the COA:

(1) The evidence in the instant appeals did not disclose any facts to support the finding that a trust was in existence (see para 38).

(2) There was no express provision in the subcontracts that specifically required the retention sums in the appeals herein to be held on trust by the employer as fiduciary, nor any clause that mandated that the retention monies were to be kept separate from the assets of the respondent. The contract between the parties did not prohibit the mixing of the monies of the respondent with the retention monies. There was no clear intention or evidence of strong conduct from the parties that indicated that the retention monies were to be accorded the status of trust monies. The written and verbal testimonies were also devoid of anything capable of suggesting that the parties had agreed for the retention sums to be held by the respondent as fiduciary for the appellants. The respondent did not take any step to segregate the retention monies and place them in a separate account, which might have indicated that the monies were to be considered as trust monies (see paras 39–42).

(3) In order for the legal relationship of trustee and beneficiary to come into existence with regard to express private trusts, three essential features had to be present, namely, certainty of words, certainty of subject and certainty of object. The retention sums in the instant appeals could not be said to be subject to a trust owing to an absence of express contractual words or conduct of the parties suggesting otherwise. Thus, the element of certainty of intention to constitute an express private trust failed. The

source of the trust property from which the retention monies were derived was not identifiable. There was consequently no certainty of subject matter. On the facts, implying a trust over the retention monies ran counter to the pari passu principle since the respondent was now insolvent and it would result in injustice to the other unsecured creditors (see paras 33 & 48).

(4) The court was very conscious of the fact that in declining to take the approach of the COA in *Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd & Anor* [2012] 3 MLJ 422, contractors and subcontractors would be exposed to high risk if their employers went into liquidation. However, similar issues had arisen in other jurisdictions such as the United Kingdom, Australia and New Zealand and reforms were undertaken to address the issues. A possible solution was to enact legislation that retention monies should be deemed as trust monies or that such monies should be placed in authorised deposit-taking institutions such as banks so that the failure to do so would invalidate the provision on retention sums in the contract (see paras 44–45).

[Bahasa Malaysia summary

Responden yang sama dalam dua rayuan ini telah secara berasingan melantik dua perayu tersebut untuk menjalankan kerja subkontrak dua projek bangunan berbeza. Subkontrak-subkontrak tersebut antara pihak-pihak membenarkan responden untuk memotong dan memegang 'retention monies' yang kena dibayar kepada perayu-perayu berkenaan dalam dua ansuran — pertama, selepas keluaran perakuan siap praktikal kontrak utama; kedua, selepas luput tempoh liabiliti kecacatan (atau keluaran perakuan memperbaiki kecacatan). Dalam kedua-dua rayuan tersebut, responden telah gagal untuk membayar wang tahanan yang ia berhutang kepada perayu-perayu tersebut. Pada masa responden melalui pembubaran sukarela, ia berhutang kepada 128 daripada subkontraktornya (termasuk perayu-perayu) wang tahanan yang tidak diabyar berjumlah RM8.2 juta. Oleh kerana responden tidak membuka apa-apa akaun bank khas untuk memegang wang tahanan ini, perayu-perayu telah memohon kepada Mahkamah Tinggi untuk memerintahkan responden mendepositkan wang tahanan yang ia berhutang kepada mereka ke dalam akaun berasingan sementara menunggi penentutan muktamad timbang tara dan/atau prosiding pengadilan. Perintah tersebut telah diberikan oleh Mahkamah Tinggi atas alasan responden telah memegang jumlah wang tahanan atas amanah untuk perayu-perayu meskipun tiada fasal nyata dalam subkontrak-subkontrak tersebut untuk pembentukan suatu amanah. Mahkamah Rayuan ('MR') telah mengetepikan perintah tersebut atas rayuan, dengan memutuskan bahawa tiada amanah boleh tersirat, kerana, antara lain, tingkah laku pihak-pihak tidak menunjukkan niat untuk membentuk amanah dan wang tahanan itu juga tidak dapat dikenal pasti secara spesifik. MR memutuskan bahawa responden hanya mempunyai obligasi kontraktual

untuk melepaskan wang kepada perayu-perayu apabila syarat-syarat untuk pelepasannya telah dipenuhi. Mahkamah Persekutuan memberikan perayu-perayu kebenaran untuk merayu terhadap keputusan MR berhubung persoalan-persoalan undang-undang berikut: (a) sama ada selagi syarat-syarat untuk pelepasan wang tahanan kepada kontraktor di bawah kontrak bangunan telah dipenuhi, undang-undang menyatakan secara tersirat bahawa majikan memutuskan wang tahanan adalah atas amanah untuk kontraktor, dan jika undang-undang tidak menyatakan sedemikian, maka sama ada suatu amanah itu wujud atau tidak bergantung kepada pembentukan kontrak itu; (b) sama ada, dalam apa keadaan, suatu amanah mungkin wujud jika majikan tidak mengetepikan wang tahanan itu dalam dana berasingan. Semasa perbicaraan rayuan, perayu-perayu berhujah bahawa memandangkan wang tahanan itu hanya boleh dipohon oleh majikan bagi tujuan pembetulan kecacatan dan bakinya perlu dibayar kepada mereka, mereka mempunyai kepentingan benefisiari dalam wang tahanan dan ia telah dinyatakan secara tersirat bahawa majikan itu telah memegang wang tersebut atas amanah untuk mereka. Responden, sebaliknya, telah berhujah bahawa tanpa peruntukan-peruntukan nyata untuk pembentukan suatu amanah, tiada amanah boleh dinyatakan. Responden juga menyatakan bahawa di bawah undang-undang insolvensi, semua pemiutang tidak bercagar dianggap sama di bawah rukun pari passu dan ia akan melanggar prinsip tersebut jika tuntutan perayu-perayu diberikan keutamaan daripada tuntutan pemiutang-pemiutang lain.

Diputuskan, sebulat suara menolak rayuan-rayuan dan mengesahkan keputusan MR:

(1) Keterangan dalam rayuan-rayuan ini tida menunjukkan apa-apa fakta untuk menyokong dapatan bahawa suatu amanah memang wujud (lihat perenggan 38).

(2) Tiada peruntukan nyata dalam subkontrak-subkontrak tersebut yang secara spesifik memerlukan wang tahan dalam rayuan-rayuan tersebut dipegang atas amanah oleh majikan sebagai fidusiari, mahu pun apa-apa fasal yang memandatkan agar wang tahanan itu disimpan berasingan daripada aset-aset responden. Kontrak antara pihak-pihak tidak melarang campuran wang responden dengan wang tahanan itu. Tiada niat atau keterangan jelas tentang tingkah laku daripada pihak-pihak bagi menunjukkan bahawa wang tahanan itu telah diberikan status sebagai wang amanah. Keterangan-keterangan bertulis dan lisan juga tiada apa-apa yang mampu untuk mencadangkan bahawa pihak-pihak telah bersetuju agar wang tahanan itu dipegang oleh responden sebagai fidusiari untuk perayu-perayu. Responden tidak mengambil apa-apa langkah untuk mengasingkan wang tahanan tersebut dan meletakkannya dalam akaun berasingan, yang mungkin menunjukkan bahawa wang itu boleh dianggap sebagai wang amanah (lihat perenggan 39–42).

(3) Bagi tujuan hubungan sah pemegang amanah dan benefisiari wujud berkenaan amanah persendirian nyata, tiga ciri-ciri utama perlu ada, iaitu, kepastian kata-kata, kepastian subjek dan kepastian objek. Wang tahanan dalam rayuan-rayuan ini tidak boleh dikatakan sebagai subjek kepada suatu amanah disebabkan oleh ketiadaan kata-kata kontraktual atau tingkah laku yang nyata oleh pihak-pihak yang mencadangkan sebaliknya. Oleh itu, elemen kepastian niat untuk membentuk amanah persendirian nyata telah gagal. Sumber harta amanah daripada wang tahanan itu diperolehi tidak dapat kenal pasti. Berikutan itu tiada kepastian hal perkara. Berdasarkan fakta, dengan menyatakan terdapat suatu amanah atas wang tahanan itu adalah bertentangan dengan prinsip pari passu kerana responden kini insolven dan ia akan menyebabkan ketidakadilan kepada pemiutang tidak bercagar yang lain (lihat perenggan 33 & 48).

(4) Mahkamah menyedari hakikat bahawa dalam menolak untuk mengambil pendekatan MR dalam kes *Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd & Anor* [2012] 3 MLJ 422, kontraktor-kontraktor dan subkontraktor-subkontraktor akan terdedah kepada risiko lebih tinggi jika para pekerja mereka telah dibubarkan. Walau bagaimanapun, isu-isu sama telah dibangkitkan dalam bidang kuasa lain seperti United Kingdom, Australia dan New Zealand dan pembaharuan telah dilakukakan untuk menangani isu-isu tersebut. Satu penyelesaian yang mungkin adalah untuk menggubal undang-undang agar wang tahanan patut dianggap sebagai wang tahanan atau wang sedemikian patut diletakkan dalam institusi pemgambilan deposit yang diberi kuasa seperti bank-bank supaya jika berlaku kegagalan untuk berbuat sedemikian akan membatalkan peruntukan berhubung wang tahanan dalam kontrak (lihat perenggan 44–45).]

Notes

For cases on retention sum held by employer, see 3(1) *Mallal's Digest* (5th Ed, 2018 Reissue) paras 4367–4368.

Cases referred to

ABB Transmission and Distributions Sdn Bhd v Sri Antan Sdn Bhd & Anor [2009] 7 MLJ 644, HC (refd)

Balfour Beatty Ltd v Britannia Life Ltd 1997 SLT 10 (refd)

CA Pacific Finance Ltd (in liquidation) and another, Re [2000] 1 BCLC 494 (refd)

Clark Taylor & Co Ltd v Quality Site Development (Edinburgh) Ltd 1981 SC 111 (refd)

Farepak Food and Gifts Ltd (in Administration), Re [2006] EWHC 3272 (Ch), Ch D (refd)

FR Absalom, Limited v Great Western (London) Garden Village Society,

Limited [1933] AC 592, HL (refd)
Geh Cheng Hooi & Ors v Equipment Dynamics Sdn Bhd and other appeals [1991] 1 MLJ 293, SC (refd)
Hunter v Moss [1994] 3 All ER 215, CA (refd)
Kumpulan Liziz Sdn Bhd v Pembinaan OCK Sdn Bhd [2003] 4 CLJ 709, HC (refd)
Lee Kam Chun v Syarikat Kukuh Maju Sdn Bhd (Syarikat Perumahan Pegawai Kerajaan Sdn Bhd, garnishee) [1988] 1 MLJ 444 (refd)
Lehman Brothers International (Europe) (a company) (in administration) and another, Re [2012] 3 All ER 1; [2012] UKSC 6, SC (refd)
Mac-Jordan Construction Ltd v Brookmount Erostin Ltd (in receivership) [1992] BCLC 350, CA (refd)
Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd & Anor [2012] 3 MLJ 422, CA (not folld)
Rayack Construction Ltd v Lampeter Meat Co Ltd (1979) 12 BLR 30, Ch D (refd)
Kayford Ltd, Re [1975] 1 All ER 604, Ch D (refd)
Tout and Finch Ltd, Re [1954] 1 All ER 127; [1954] 1 WLR 178, Ch D (refd)
Wates Construction (London) Ltd v Franthom Property Ltd (1991) 53 BLR 23, CA (refd)
White v Shortall [2006] NSWSC 1379, SC (refd)
Wilmot v Alton and another [1897] 1 QB 17, CA (refd)
Yeong Ah Chee v Lee Chong Hai & Anor and other appeals [1994] 2 MLJ 614, SC (refd)
Yew Sang Hong Ltd v Hong Kong Housing Authority [2008] HKCA 109; [2008] BLR 563 (refd)

Appeal from: Civil Appeal Nos W-02(NCC)(A)-945–05 of 2016 and W-02(IM)(NCC)-887–05 of 2016 (Court of Appeal, Putrajaya)

Lim Wai Loon (Rohan Arasoo and Teoh Yen Yee with him) (Harold & Lam Partnership) for the appellant.
Chong Hooi Yin (Muhammad Iqram bin Zulkupri with him) (Azman Davidson & Co) for the respondent.

Richard Malanjum Chief Justice (delivering judgment of court):

INTRODUCTION

[1] The present appeals arise out of common issues of law in relation to actions brought by two different plaintiffs against the same defendant. The cases related to these appeals were heard together before the first instance court and the Court of Appeal. Each court rendered one judgment respectively. Thus, the appeals before us are Appeal No 130 and Appeal No 131 again heard together due to the common issues of law involved.

Appeal No 130

[2] The appellant in Appeal No 130 (plaintiff at the High Court) was the respondent's (defendant at the High Court) subcontractor for a mixed development project in Sungai Buloh, Selangor for the sum of RM9,789,815. Pursuant to cl 16.3 of the subcontract between the parties, a sum of RM489,490.75 was retained by the respondent as retention monies. The retention monies were to be released by the respondent to the appellant in two tranches: firstly, upon the issuance of the certificate of practical completion ('CPC') of the main contract and secondly, upon the expiry of the defect liability period ('DLP').

[3] Although the CPC was issued on 30 May 2013 and the DLP lapsed on 30 August 2015, the respondent did not release the first and the second tranches of the retention monies to the appellant.

Appeal No 131

[4] The appellant in Appeal No 131 (plaintiff at the High Court) was engaged as the respondent's (defendant at the High Court) subcontractor for a project in Johor for the sum of RM17,734,455,55. As in Appeal No 130, cl 16.3 of the subcontract between the appellant and respondent in Appeal No 131 provided for a sum of RM886,723 to be retained as retention monies where the first moiety was to be released by the respondent upon the issuance of the CPC and the second moiety was to be released upon the issuance of the certificate of making good defects ('CMGD') of the main contract works.

[5] For Appeal No 131, the retention monies were never released to the appellant as well.

[6] On 2 November 2015, a creditors' meeting was held and a special resolution was passed for the voluntary winding up of the respondent.

[7] Based on the statement of affairs on the respondent as at 8 October 2015:

(a) the total debt owed to the unsecured creditors of the respondent was RM91,878,716.62;

(b) the estimated net realisable value of the assets of the respondent was RM18,857,298 with cash at bank at RM547,786;

(c) the respondent's liabilities exceeded assets by RM73,019,479;

(d) there are about 250 creditors, out of which around 128 are creditors claiming retention sums; and

(e) the total amount owed to creditors for retention monies was RM8,230,087.61. This included the total amount of retention sums owed to the two appellants in the present appeals.

[8] The respondent did not open any bank account for the retention monies including those for the appellants in these appeals. For convenience, in this judgment both the appellants in these two appeals are collectively referred to as the appellants.

BEFORE THE HIGH COURT

[9] As alluded to above, the appellants respectively instituted an action at the High Court seeking leave to commence and proceed with court, arbitration and/or adjudication proceedings against the respondent and for the respondent to be ordered to preserve the retention sums in a separate account pending the final determination of the arbitration and/or adjudication proceedings.

[10] Relying on the Court of Appeal decision in *Qimonda Malaysia Sdn Bhd (in liquidation) v Sediabena Sdn Bhd & Anor* [2012] 3 MLJ 422, the High Court held that the retention sums were being held on trust by the respondent. The basis of such finding was that while there was no express clause providing for the creation of a trust over the retention monies, a trust could still arise due to the fact that there was a provision for the release of the retention monies upon any rectification work on any defect completed and since no notice was received from the respondent of any defect. Thus, the High Court granted the reliefs sought for by the appellants.

BEFORE THE COURT OF APPEAL

[11] On appeal, the Court of Appeal reversed the High Court decision. It held that there could be no trust because of the lack of an express clause or clear conduct from the parties as well as the retention monies were never segregated.

[12] The Court of Appeal took the view that a trust cannot be implied purely from the nature and purpose of retention monies per se, and that the concept of a trust is not inherent in the use of the word 'deductions'. It went on to hold that most construction contracts do not operate via a trust, unless otherwise expressly stated, but at the level of contract and debt (see: *Re Farepak Food and Gifts Ltd (in Administration)* [2006] EWHC 3272 (Ch)). A mere debt is a chose in action and does not confer any beneficial right in retention monies on the basis of trust.

[13] The Court of Appeal went on to distinguish between these appeals and that of the decided cases, both local and foreign, based on the facts (see: *Rayack*

Construction Ltd v Lampeter Meat Co Ltd (1979) 12 BLR 30, *Mac-Jordan Construction Ltd v Brookmount Erostin Ltd (in receivership)* [1992] BCLC 350, *Kumpulan Liziz Sdn Bhd v Pembinaan OCK Sdn Bhd* [2003] 4 CLJ 709). In those cases, there was an express clause in the contracts providing for the employers to hold the retention monies on trust for the contractors in a fiduciary capacity. But where there is no such or similar provision, a trust ought not to be construed as subsisting and more so when the conduct of parties does not lend itself to such an inference. The Court of Appeal also observed that there is no general proposition of law in a building contract that retention monies are, as a rule, held by way of trust between an employer and a contractor.

[14] While the Court of Appeal accepted the principle that a trust may exist without the necessity of having to use express words relating to trusts to create it (see: *Re Kayford Ltd* [1975] 1 All ER 604), it affirmed the principle that a trust fund may not come into existence just because a contractual clause provides so. Indeed it was pointed out by the Court of Appeal that there was a clear difference between an intention to create a trust and the creation of a valid trust. Thus, cl 16.3 and the relevant provisions in the Appendix related to the said clause could at best be said to have created a contractual obligation on the part of the employer to retain the monies in favour of the subcontractor and to release them when the conditions have been satisfied. Any failure by the employer to comply with such obligation would be a contractual default.

[15] Another principle of law mentioned by the Court of Appeal is that traditionally under the law of equity and trusts, property must be separately identifiable in order to infer a trust so that there would be a tangible subject matter upon which the trust could be impressed.

[16] And it was suggested by the Court of Appeal that there should be set up a statutory mechanism for retention monies to be kept separately on trust for subcontractors to ensure the protection of their interest, similar to what has been introduced in other jurisdictions.

ISSUES BEFORE THIS COURT

The leave questions

[17] On 26 October 2017, this court granted leave to appeal in relation to the following questions of law:

(i) where a building contract provides that a certain percentage of the certified sum for work done by a contractor is to be retained by the employer until the conditions for the release of the sum retained ('retention sum') are met:

(a) is it implied by law that the retention sum is to be held in trust by the employer for the benefit of the contractor; or

(b) is it a matter of construction (interpretation of contract) whether or not the retention sum is to be held in trust by the employer for the benefit of the contractor?

(ii) where in a building contract there exists an agreement (whether arising by implication of law or upon construction of the contract) that the retention sum is to be held in trust by the employer for the benefit of the contractor, can the trust of the retention sum be constituted without the employer first appropriating and setting aside the money as a separate trust fund?

THE APPELLANTS' SUBMISSION

[18] The appellants assert that:

(a) in a construction contract retention monies are trust monies held by an employer in a fiduciary capacity, as trustee for the benefit of the contractor. The employer can only utilise these monies for the limited purpose of rectifying any defects and the balance is to be paid to the contractor;

(b) since retention monies are to be applied only for a particular purpose, it follows that the contractor has a beneficial interest in them. Thus, it must be implied that retention monies are held by the employer on trust for the benefit of the contractor; and

(c) there is no requirement that retention monies should first be separated from the assets of the employer if by implication they are considered trust monies.

THE RESPONDENT'S SUBMISSION

[19] The respondents on the other hand contend that:

(a) the Court of Appeal in *Qimonda* did not reach a conclusion whether there was an implied trust before finding that the High Court was correct in law and in fact in holding that the retention monies 'by their very nature and purpose are trust monies';

(b) although it is indeed a common feature in many contracts for a percentage of the amount certified in interim payments to be deducted by the employer as retention monies, this common feature is by no means a universal feature and does not assist in a case where the words do not appear to show that retention monies by their very nature are held in a fiduciary capacity;

(c) in the *Qimonda* case the Court of Appeal reliance on the cases of *FR Absalom, Limited v Great Western (London) Garden Village Society, Limited* [1933] AC 592, *Lee Kam Chun v Syarikat Kukuh Maju Sdn Bhd (Syarikat Perumahan Pegawai Kerajaan Sdn Bhd, garnishee)* [1988] 1 MLJ 444, *Re Kayford*, *Geh Cheng Hooi & Ors v Equipment Dynamics Sdn Bhd and other appeals* [1991] 1 MLJ 293, *ABB Transmission and Distributions Sdn Bhd v Sri Antan Sdn Bhd & Anor* [2009] 7 MLJ 644 and *Kumpulan Liziz Sdn Bhd v Pembinaan OCK Sdn Bhd* [2003] 4 CLJ 709 was misplaced. Those cases do not support the proposition that retention monies are trust monies. Thus, the categorical position in *Qimonda* that 'retention monies by their very nature and purpose are trust monies held by the Employer or main contractor for the contractor or subcontractor' is without basis;

(d) the subcontract agreement in the instant appeals do not contain an express trust provision. There are also no circumstances from which an implied trust can be held to arisen;

(e) generally a simple advance payment of money for a particular purpose is not enough to indicate that the recipient intended to hold it on trust for the payer;

(f) there is a distinction between a trust and an obligation to create one;

(g) the Court of Appeal in the instant cases correctly departed from *Qimonda* on the following points:

(i) it is not sufficient to create a trust in the absence of an express clause or clear intention;

(ii) the subcontractors do not in the absence of a trust enjoy beneficial interest in the retention monies as their claim is in the nature of a debt; and

(iii) if the proposition in *Qimonda* is accepted by this court it would amount to enacting a new and general principle of law where a trust is implied by operation of law in all construction contracts where there is a deduction as retention monies;

(h) the Court of Appeal in *Qimonda* did not take into account the subsequent English Court of Appeal decision in *Mac-Jordan* which held that since there was no setting aside of the fund before the employer went into receivership, there were no trust assets capable of identification. Under the law of equity and trusts, trust property must be identifiable; and

(i) to allow the appellants to exercise their right to recover such retention sums would disadvantage the remaining 126 subcontractors who have similar claims let alone the other general unsecured creditors. The

application of the pari passu rule in Malaysia is a statutory requirement and the maxim he who is first has the strongest right simply has no place in insolvency law where the established rule of equality of treatment applies.

DECISION OF THIS COURT

[20] In the construction industry the contract between an employer and a contractor usually has a provision that gives the employer the right to retain certain percentage from the interim sums certified payable to the contractor for work done. Such a contractual provision may also stipulate the purpose of the retention sum, its management and keeping pending usage or release, and the time for its actual release to the contractor. Therefore, being a creature of a contractual provision, the legal status of a retention sum, including its management pending release to the rightful payee, is very much subject to the term or terms as stipulated in such a provision.

[21] In Appeal No 130, the subcontract entered into between the appellant and the respondent contained cl 16.3 which reads:

> Unless otherwise stated in the Appendix, each and every payment for Interim Claim shall be subjected to a 10% retention sum to the maximum limit of 5% of the Sub-Contract Price.

[22] The Appendix to the conditions of the subcontract aforementioned which relates to the release of retention sum provides that:

> [The] 1st moiety shall be released upon issuance of Certificate of Practical Completion (CPC) of the Main Contract Works and will be forward a copy accordingly;
>
> [The] 2nd moiety shall be released upon issuance of the Certificate of Completion of Making Good Defects (CMGD) of the Main Contract Works and will be forward a copy accordingly.

[23] In Appeal No 131, the subcontract entered between the appellant and the respondent also has an identical provision as cl 16.3.

[24] However, the Appendix to the Conditions of subcontract provides that 2.5% of the retention sum will be released to the appellant upon the issuance of the CPC while the balance is to be returned upon the end of the DLP.

[25] It can therefore be seen that cl 16.3 and the Appendix thereto clearly provide the right to retain the retention sums and when to release them. What then is the status in law of retention sums in Malaysia? Is it under trust or just

A money due and owing in the event that it is not released as provided for in cl 16.3 and in the Appendix of the subcontract?

[26] As alluded to above, retention money is money withheld by the employer from the sum otherwise certifiable to the contractor. It serves as a safeguard against the possibility of the contractor's failure to complete the works and against defective work (see: Powell-Smith, Vincent, *The Malaysian Standard Form of Building Contract (PAM/ISM 69*, (Singapore: Malayan Law Journal, 1990), at p 147; LexisNexis, *Halsbury's Laws of England*, Vol 6, 2011, 5th Ed, *Building Contracts*, '3 Certification and Remuneration' [347]). The amount retained is usually a small fraction of the work properly executed by the contractor. It is accumulated by deducting the appropriate percentage from the valuation of work at each interim payment (see: Chappell, David, *Construction Contracts: Questions and Answers*, 2nd Ed, (England: Routledge, 2010) at p 168).

[27] The status of retention sum under English law is circumscribed by the standard-term building contracts of the United Kingdom. In such a term, the employer undertakes to hold the retention sum on trust for the contractor. For instance, cl 30.5.1 of the UK standard construction contract JCT 1998 provides that the 'employer's interest in the retention is fiduciary as trustee for the contractor and for any nominated sub-contractor'. The effect of such a contractual provision is to impose upon the employer a personal obligation to appropriate and set aside as a trust fund the amount of retention money withheld. If this is successfully done, the contractor's claim to the retention money takes priority over the employer's general creditors in the event of the employer's insolvency, and a liquidator of the employer would be obliged to hand over the retention fund in full to the contractors and subcontractors involved.

[28] Thus, in the United Kingdom when a solvent employer neglects to perform its obligation as mandated by such clause the contractor may apply for a mandatory injunction against such employer. The employer is then compelled to set aside the retention sum in order to protect the contractor against the employer's insolvency (see: *Rayack Construction Ltd v Lampeter Meat Co Ltd*; *Wates Construction (London) Ltd v Franthom Property Ltd* (1991) 53 BLR 23).

[29] However, the position would be different where the contractor had gone into liquidation without having set aside as a trust fund the amount of retention money withheld. The question of trust does not arise in such a situation since there is no res to which the trust can attach. Thus, if the employer merely deducts the contractually agreed percentage from interim payments which he would have otherwise paid to the contractor, there is only

a withholding of payment instead of the setting up of a distinct fund. There would consequently be no trust asset to which the contractor could have recourse in the event of the employer's insolvency (see: Goode, Roy, *Principles of Corporate Insolvency Law* (4th Ed, London, Sweet & Maxwell, 2001), para [44] at pp 214–215).

[30] It is therefore essential under English law that where parties have agreed by contract for the retention monies to be impressed with a trust, it is vital for the trust to have been established before the employer's insolvency. Otherwise, the money will form part of the monies to be distributed pari passu in the winding-up, and the contractor will be unsecured (see: Dennys, Nicholas and Robert Clay, *Hudson's Building and Engineering Contracts* (13th Ed, London, Sweet & Maxwell, 2015) para [5-068] at pp 698–699). Such a situation arose in *Mac-Jordan Construction Ltd v Brookmount Erostin Ltd* and *Wilmot v Alton and another* [1897] 1 QB 17. In those cases it was found that there was no proprietary interests in the respective building retention funds. There were no identifiable assets that could be the subject of the established mandatory and unconditional personal obligation (See: Worthington, Sarah, *Proprietary Interests in Commercial Transactions* (Oxford: Claredon Press, 1996), at p 190, footnote [16]).

[31] The Scottish position appears to be similar as that of English position. Even if the contract provides a mechanism whereby the retention deducted by the employer is to be held on trust on behalf of the contractor, the existence of express terms per se is insufficient to create a trust without any other actions (such as the setting aside of the monies) on the part of the employer (see: *Clark Taylor & Co Ltd v Quality Site Development (Edinburgh) Ltd* 1981 SC 111 and *Balfour Beatty Ltd v Britannia Life* (1997) SLT 10. This would mean that in Scotland under the Standard Building Contract and the Design and Build Contract, if an employer becomes insolvent, then, in respect of the payment of retention fund that has been deducted, the contractor may find themselves in no better position than other ordinary creditors (See: MacRoberts, *MacRoberts on Scottish Construction Contracts* (3rd Ed, UK: John Wiley & Sons, 2015) at pp 225–226).

[32] Thus, gleaned from the judicial decisions in the United Kingdom and Scotland and the views expressed by learned authors on retention sum the legal principles that may be crystalised are these:

(a) an agreement must employ sufficiently unambiguous terms to show that a trust is created with the contractor or subcontractor as the beneficiary (see: Davis, Richard, *Construction Insolvency: Security, Risk and Renewal in Construction Contracts* (5th Ed, London: Sweet & Maxwell, 2014), para [10-006] at pp 389–390; *Re Tout and Finch Ltd* [1954] 1 All ER 127; [1954] 1 WLR 178 per Wynn-Parry J);

A (b) while an explicit clause creating a trust may be of help it does not mean that an absence of such a clause negates the existence of a trust;

(c) there is no presumption that monies held in a separate account must necessarily be held on trust;

B (d) at any rate, each case depends on the parties' specific intention as expressed in the relevant construction contract (see: Bailey, Julian, *Construction Law Volume (II)*, (England: Informa Law (Routledge), 2011) at p 898); and

C (e) even where there is a fiduciary relationship between an employer and a contractor, not every fiduciary is a trustee. Such a person can have obligations towards another's property even though it may not be vested in him. The nature and extent of a fiduciary's duties are variable and depend on the circumstances in each case.

D

[33] Now, reverting to the basics, it is a settled principle of law that in order for the legal relationship of trustee and beneficiary to come into existence as regards express private trusts, three essential features must be present. They are (a) certainty of words; (b) certainty of subject; and (c) certainty of object (see: E Tucker, Lynton, et al, *Lewin on Trusts* (19th Ed, London: Sweet & Maxwell, 2015) at p 102; Haley, Michael and Lara McMurty, 'The Three Certainties', *Equity & Trusts* (5th Ed, London: Sweet & Maxwell, 2017) at p 44); *Yeong Ah Chee v Lee Chong Hai & Anor and other appeals* [1994] 2 MLJ 614 at p 624). Under a trust, a party holding title to property is subject to an obligation to F keep or use the property for the benefit of another party. The person holding the property for another's benefit is called a trustee, while the person benefiting from the trust is called the beneficiary. The property covered by the trust is the trust property.

G **[34]** In *Qimonda* the Court of Appeal found that there was a trust of the retention sum despite the absence of express trust clause or words to that effect in the contract and there were no unusual terms as well. In that case, no fund was set aside before the liquidation, nor had the contractor requested it. Although the court held that the 'requisites' of a valid trust were present, there H seemed to be no evidence of either intention or trust property. While the agreement only demonstrated a contractual scheme and nothing further was said about the correspondence yet the court held that they manifested the clear intention of the parties. Further, the case of *Re Kayford* was relied upon as authority for the proposition that it was not necessary to set money aside. But, I with respect, *Re Kayford* was decided in the context of payment actually received from customers paying for goods in advance. In *Qimonda* there was no payment by the contractor that could constitute trust property. There was only the agreement that the employer would release the retention sum to the contractor conditional upon the final correction of defects (see: Davis, Richard,

Construction Insolvency: Security, Risk and Renewal in Construction Contracts (5th Ed, London: Sweet & Maxwell, 2014) para [10-006] at pp 389–390). Accordingly, we find it difficult to sustain the decision in *Qimonda* in the light of the settled principles in trust law.

[35] Having read the judgment of the Court of Appeal in these appeals, we are inclined to agree with the reasons given therein. We find that the approach is generally consistent with the English approach. As elucidated above, English authorities require that if retention monies are to be impressed with trust the contract should identify by clear wordings that the retention monies are held in trust and for the trust fund to be established before the insolvency. Such approach would appear to be consistent as seen from the decisions in *Rayack Construction Ltd v Lampeter Meat Co Ltd* which was followed in both *Wates Construction (London) Ltd v Franthom Property Ltd* and *Mac-Jordan Construction Limited v Brookmount Erostin Ltd*. While it may appear that the English approach is strict, it is still preferable for it tempers the risk of uncertainty and the likely competing claims that would ensue if the *Qimonda* approach is adopted. It also avoid the undesirability of not applying the assets in the hands of liquidators *pari passu* (except where monies are clearly identified as trust monies relating to a trust fund established before the insolvency of the employer) (see: Dennys, Nicholas and Robert Clay, *Hudson's Building and Engineering Contracts*, op cit para [5-068] at p 699).

[36] We would also say that the requirement to keep a retention sum segregated from and unmixed with other monies of an employer is very much a significant indicator of the parties' intention. Although in *Qimonda* the Court of Appeal relied on *Absalom* we find upon further consideration in that case the House of Lords did not go so far as to say that retention monies should be held in a fiduciary capacity notwithstanding the absence of any express trust provision in a contract.

[37] We note that the Hong Kong Court of Appeal had a similar issue before it in the case of *Yew Sang Hong Ltd v Hong Kong Housing Authority* [2008] HKCA 109; [2008] BLR 563 at paras [52]–[59]. The court took the English approach in deciding on the issue declining to adopt the reasoning in *Qimonda*. It preferred to uphold the pari passu principle when it said this at para 13: 'to allow a creditor a restitutionary remedy in the interest of 'doing justice' in a specific case would only lead to that creditor jumping the queue of unsecured creditors and so bring about injustice in everyone else's case'.

[38] Accordingly, we have no good reason to depart from the current approach adopted in the common law jurisdictions. As such, in these appeals our perusal of the evidence did not disclose any facts to support the finding that a trust was in existence.

A **[39]** Besides the contractual provisions of cl 16.3 and the Appendix of the Conditions of subcontract reproduced hereinabove, there is no express provision specifically requiring the retention sums in Appeal No 130 and Appeal No 131 to be held on trust with the employer as the fiduciary.

B **[40]** There was also no clause mandating that the retention monies were to be kept separate from the assets of the respondent. The contract between the appellants and the respondent did not prohibit the mixing of the monies of the respondent with the retention monies.

C **[41]** We are also unable to discern any clear intention or evidence of strong conduct from the parties that indicated the retention monies should be accorded the status of trust monies. The written and verbal testimonies were similarly devoid of anything capable of suggesting that the parties had agreed
D for the retention sums to be held by the respondent as fiduciary for the appellants.

[42] Indeed the respondent did not take any additional steps such as segregating the retention sums that might then indicate that the retention
E monies should be considered as trust monies. In fact there is no evidence of a separate account into which the retention monies were allocated. Such step would have allowed for easier identification of the retention sums as trust monies.

F **[43]** We have not overlooked that there is an emerging trend of judicial thought which posits that monies forming part of a larger bulk do not fail to be impressed with a trust for uncertainty of subject matter simply because they have not been isolated from the general assets of the insolvent company, if the
G monies are capable of identification as a proportion of the whole fund. This proposition which rests on the 'fungible' nature of money is borne out by cases such as *Hunter v Moss* [1994] 3 All ER 215, *Re Lehman Brothers International (Europe) (a company) (in administration) and another* [2012] 3 All ER 1; [2012] UKSC 6, *White v Shortall* [2006] NSWSC 1379 and *Re CA Pacific Finance Ltd*
H *(in liquidation) and another* [2000] 1 BCLC 494. In our considered opinion, the principle in the aforementioned authorities has no bearing on the present appeals in view of the factual matrix in these cases.

I **[44]** We are very conscious that in declining to take the approach as in *Qimonda* contractors and subcontractors are exposed to high risk in the event of the employers going into liquidation. However, in other jurisdictions such as the United Kingdom, Australia, and New Zealand similar issue also arose. Reforms were undertaken to address the issue.

[45] One possible solution is to enact legislation enabling retention sums to be placed in authorised deposit-taking institutions such as banks. Failure to do so would invalidate the provision on the retention sum in the contract. Another solution may be to legislate that retention sums should be deemed as trust monies.

[46] In Australia, a mandatory deposit scheme was introduced in New South Wales. In Western Australia and the Northern Territory, it is legislation that prescribes for the creation of a trust where the parties do not provide otherwise in their contract (see: Australia, Parliament of Australia, 'Chapter 10: A Statutory Construction Trust', *Senate Standing Committees on Economics: Insolvency in the Australian Construction Industry*, 8 February 2019 https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Insolvency_construction/Report/c10).

[47] Another country, New Zealand recently implemented a statutory regime where a trust is imposed over retention monies regardless of whether they are held in a separate trust fund. Under the New Zealand model, the mixing of retention monies with other sums has no bearing on their status as trust monies (see: New Zealand, Ministry of Business, Innovation and Employment, Construction Contracts Amendment Act 2015, 8 February 2019).

[48] In summary, the retention sums in the instant appeals cannot be said to be subject to a trust owing to an absence of express contractual words or conduct of the parties suggesting otherwise. Thus, the element of certainty of intention to constitute an express private trust fails. Furthermore, the source of the trust property from which the retention sums may be derived is not identifiable. There is consequently no certainty of subject matter. On the facts, implying a trust over the retention monies also runs counter to the pari passu principle now that the respondent is insolvent and would result in injustice to the other unsecured creditors.

[49] For the reasons stated above, question (i)(a) of the leave question is answered in the negative. leave question (i)(b) is answered in the affirmative while leave question (ii) is answered in the negative.

[50] We therefore dismiss these appeals with costs. The decisions of the Court of Appeal in both appeals are affirmed.

A *Appeals unanimously dismissed abd decision of COA affirmed.*

Reported by Ashok Kumar

B

C

D

E

F

G

H

I